TC07160

VAT-valid invoice or not-not-whether HMRC's decision not to accept other evidence, in the absence of valid VAT invoices was reasonable-yes-appeal dismissed

FIRST-TIER TRIBUNAL **Appeal number: TC/2016/07093**

TAX CHAMBER

BETWEEN

SYMPHONY HOTELS & LEISURE LIMITED **Appellant**

-and-

THE COMMISSIONERS FOR

HER MAJESTY'S REVENUE AND CUSTOMS **Respondents**

TRIBUNAL: JUDGE ANNE SCOTT

Sitting in public at George Street, Edinburgh on Thursday 18 April 2019

Philip Simpson, QC, for the Appellant

Mrs E McIntyre, Officer of HMRC, for the Respondents

DECISION

INTRODUCTION

1. The matters under appeal are HMRC's decisions to:

   (a) Amend the appellant's Value Added Tax ("VAT") return for the period 1 November 2014 to 31 January 2015 (01/15) thereby reducing the amount of input tax claimed and resulting in no VAT credit and an amount due by the appellant of £48,304.80; and

   (b) Issue assessments for periods 10/13 to 01/16 (excluding 01/15) relating to the recovery of VAT on invoices purporting to relate to a supply of labour. As a result of those assessments the total of VAT due is £459,479.

2. The appellant states that the issue is:

   > "… whether the Appellant obtained supplies of labour, human resources and related services from certain third parties so that the Appellant is entitled to deduct input VAT charged by and paid to those third parties."

3. Conversely, HMRC argue that the issue is:

   > "Whether or not the evidence held by the Appellant is sufficient to allow them to recover amounts shown on invoices as input tax."

4. I find that the issue is whether or not there are valid invoices in respect of a taxable supply to the appellant in which case the appeal succeeds. If there are no valid invoices, then whether HMRC's decision that, in the absence of valid invoices, their decision not to exercise their discretion to accept alternative evidence as to whether there had been a tax supply was correct.

5. I had one Bundle which included witness statements, documents, correspondence and authorities. I heard evidence from Mr Sheffield, the sole director of the appellant. I also heard evidence from Miss Drummond, the compliance officer of HMRC, who issued the amendment and the assessments.

Findings in Fact

6. During the periods which are the subject matter of this appeal, the appellant ran three hotels, one of which closed down at some point in the period (possibly in October 2014).

7. In 2013, apparently because of the economic climate, the appellant reviewed its business practices and made contact with an outsourcing business.

8. It is not possible to accurately identify precisely what that business was.

9. All that I can find as a fact is that Mr Sheffield contacted and dealt with a Mr Howard Jones.

10. In his witness statement, Mr Sheffield indicated that he had been recommended to a business called Quadrant 2. In fact there was produced an email dated 11 September 2013 from Howard Jones to Mr Sheffield referring to a telephone call and setting out an overview of what was required to transfer the payroll services to what was described as "The Outsourcing Provider". That provider was not identified.

11. Mr Jones described himself as a partner in Gatwick Outsourcing and GoGroup which were trading styles of the Gatwick Outsourcing Partnership. Another five companies were identified as being part of that Group. One, Gatwick Outsourcing Bureau Ltd, was subsequently identified to HMRC by the appellant's accounts staff (see paragraph 19 below).

12. On 1 October 2013, Mr Sheffield signed an Employment Service Agreement ("the First Agreement") with a company called Mead Outsourcing Limited ("Mead") which recorded the transfer of all of the appellant's staff to Mead, under the TUPE provisions, with immediate effect. Mr Jones and Mr Sheffield appear to have signed it on that day.

13. In summary, the First Agreement provided that, notwithstanding the transfer to Mead, the appellant would retain responsibility for day to day direction, control and supervision of the staff and Mead would administer the payroll return for an administration fee. Clause 19.2 provided that Mead could not assign, novate or otherwise dispose of all or any of its rights and obligations without the prior written consent of the appellant.

14. The First Agreement referred to a Deed of Transfer between the appellant and Mead whereby the appellant assigned and transferred the contracts of employment of the staff to Mead. According to Mr Sheffield, Mr Jones signed that document for Mead on the same day. The signature is similar to, but not identical to, the signature on the First Agreement.

15. The last agreement signed that day between Mead and the appellant was an Agency Payment Agreement whereby the appellant undertook to pay the staff as agent for Mead. The signature for Mr Jones is quite different to that on the other two. In fact that agreement was never implemented.

16. On a compliance visit conducted by HMRC on 28 August 2014 Officer Drummond was told that the payroll for staff had been outsourced. She noted that the appellant was the recipient of supplies of invoices for labour which quoted amounts of VAT and against which input tax credit was claimed. The invoices were issued by "Quadrant Services (UK)". No VAT number for that company is quoted but the invoices detail in a box:

> "Quadrant Group acting as agents for:
>
> UX-Ray LIMITED
>
> VAT: 119 9502 01".

The bank account reference at the bottom of the invoice was in the name of "Mead Outsourcing".

17. Although, at that stage, Officer Drummond knew nothing about the First Agreement she quickly became concerned because it was immediately apparent that the staff were wholly unaware that their contracts of employment had been outsourced. Indeed they were still issuing new contracts of employment in the appellant's name and have continued to do so after her visit.

18. The staff confirmed that all of the staff had received tax rebates from HMRC at the end of the 2013/14 tax year as HMRC had believed them to only have been employed until September 2013. The accounts staff confirmed that the PAYE reference quoted on their P60s was that for Red Management Catering Limited. On contacting HMRC, HMRC had confirmed to the staff that that company had ceased to exist in 2011.

19. The accounts staff pointed out that the current payslips had no information as to the employer but they did have paperwork and/or payments to and from the following companies, namely:

> Furners Management Ltd,
>
> Gatwick Outsourcing Bureau Ltd,
>
> Gatwick Outsourcing Group Ltd,
>
> Mead Outsourcing Ltd,

Quadrant Services Ltd,

Red Management Catering Ltd, and

UX-Ray Limited.

20. On 26 March 2015, HMRC issued a letter, headed "**WARNING"**, to the appellant intimating that UX-RAY LIMITED was deregistered for VAT purposes with effect from 1 December 2014. HMRC warned about fraud and issued their Notice about due diligence and what sort of checks companies such as the appellant should make.

21. Quadrant Services (UK) certainly issued invoices referring to, and using, the VAT registration number ("VRN") for UX-Ray Limited after 1 December 2014 and into 2015 and the appellant claimed the input tax. (I observe that HMRC's spelling of the trader's name is identical to that on the VAT certificate dated 24 July 2013, as it should be, and different to that on the invoices.)

22. Mr Sheffield confirmed that he was aware that an unregistered business cannot charge VAT.

23. Mr Sheffield stated that the only action that he had taken on receipt of that letter was to speak to Mr Jones who had reassured him that everything was in order. He had apparently believed him. He had undertaken no further due diligence.

24. At some unspecified date, Mr Sheffield told Mr Jones that HMRC had asked questions about the invoices and, on 2 April 2015, Mr Jones emailed HMRC, apparently at Mr Sheffield's request offering his assistance. HMRC did not respond to him. Mr Jones' email described him as writing from "Quadrant Services, a trading name of the Quadrant Partnership (UK)". Of course that is not the name on the invoices, and nor is it any of the names quoted by Mr Sheffield.

25. On 7 May 2015, Officer Dick from HMRC's Fraud Investigation Service, met with Mr Sheffield because of concerns about the VAT return with input tax claims for the 01/15 quarter which included invoices issued after UX-Ray LIMITED was deregistered.

26. At that meeting Mr Sheffield furnished HMRC with further labour invoices issued by Quadrant Services (UK) which were in the same format as previously (see paragraph 16 above) but those invoices stated that Quadrant Group were acting as agents for "Decent Solutions Limited VAT: 103 6741 41".

27. On 7 September 2015, Officer Dick wrote to the appellant stating that its employer and business records had been selected for a compliance check and pointed out that the VAT invoices were invalid because the supply of labour was by Mead.

28. On 17 December 2015, Officer Kinnear of HMRC intimated to the appellant that an enquiry would be opened into the company tax return for the period ended 2 April 2014.

29. On 23 February 2016, the officers visited the appellant and, apart from examining the books and records, explained:

(a) That HMRC's company tax records showed an intent to strike off dated 4 April 2014 (it was subsequently confirmed on 17 March 2016 that Companies House had issued a compulsory winding up notice to the appellant on that date but steps were then taken to halt the process), and

(b) That HMRC were concerned, not about fraud by the appellant, but about possible links with wider fraud.

30. I had the benefit of the detailed notes of that meeting which Mr Sheffield attended accompanied by his accountant. It is recorded that he provided information about payroll and staff and specifically:

> (a) "7. ix) There have been no problems with payroll in recent years. This has been outsourced to a payroll service, Red Management Catering."
>
> (b) "7. xv) The figure in the accounts for agency labour is the payments to Quadrant, which is the company who handles the payroll. The employees were all paid off…and taken on by the new payroll administered by Quadrant. They are regarded as an agency but it is the company who recruits and controls the employees."
>
> (c) "11. CK asked MS why the company payroll show (sic) no current employees and MS explained that all employees, including himself, were transferred to the payroll provider payroll in 2013."

31. Mr Sheffield thereafter provided the further information requested by HMRC including copies of further invoices.

32. On 7 April 2016 Officer Dick wrote to Mr Sheffield reiterating that the invoices for January 2016 issued by Quadrant Services (UK) acting as agents for Decent Solutions Limited were not valid VAT invoices.

33. I can see that by January 2016 the bank reference at the bottom of the invoices was in the name of "Dedicated Outsourcing Limited" instead of "Mead Outsourcing" and at a different address but that address was the same address as that for Gatwick Outsourcing Bureau Limited (see paragraphs 11 and 19 above). Curiously, the bank details and sort code remained the same.

34. Also on 7 April 2016, Officer Dick wrote to Mr Sheffield with a "Notification of Tax Loss" letter in standard terms explaining fraud and the "Kittel" principle, with which most readers of this decision will be familiar, and pointing out that at least one of the participants in the supply chain with Decent Solutions Ltd had failed to meet its VAT liability. Mr Sheffield was strongly advised to verify the VAT status of his labour providers. He did not. (There was an EC VAT number validation in the Bundle for Decent Solutions Limited but it is dated many months after the periods with which this appeal is concerned and Mr Sheffield did not recall it).

35. On 17 May 2016, Officer Drummond wrote to the appellant intimating that an assessment would be issued for the VAT incorrectly claimed because there were no valid VAT invoices and there were links to fraudulent evasion of VAT.

36. On 26 May 2016 a Closure Notice was issued with no amendments to the company tax return.

37. The following day Mr Sheffield wrote to HMRC complaining that he had no knowledge of fraud and that he had paid the invoices in good faith. Correspondence ensued, culminating in this appeal.

Reasons for the Decision

38. In summary, for the reasons outlined below, I found Mr Sheffield's evidence to be neither credible nor reliable. His evidence was riven with inconsistency.

39. Paragraph five of the appellant's Skeleton Argument reads:

> "The issue in the present case arises because of errors in the documentation relating to the supplies. Specifically, the outsourcing contract and related documents identify Mead Outsourcing Limited ('Mead') as the Appellant's contracting party, whereas the VAT invoices identify other companies, albeit in the same corporate group as Mead ('the Quadrant Group'), to be the supplier, and include the relevant company's VAT registration number".

40. No documentary evidence has been produced in relation to the alleged corporate group. Mr Sheffield's evidence did not assist.

41. As I indicate at paragraph 10 above, Mr Sheffield had argued in his witness statement that business associates had recommended an outsourcing business called Quadrant 2 and his main contact was Howard Jones. The witness statement at paragraphs 3 and 4 went on to state that he had done due diligence by researching on the internet for "the parent company", speaking to other business owners and researching on the internet as to which other companies used that service.

42. When speaking to those paragraphs in his oral evidence, he said that the parent company was Quadrant Services Limited. He confirmed that he had looked at their website and done "a lot" of due diligence but was wholly unable to explain why he had referred to Quadrant 2.

43. By contrast at paragraph 6 of his witness statement he said:

> "I understood that Mead Outsourcing Limited were (sic) the parent company and it was part of the Quadrant Group of companies – this was explained to me at the time. I understand that many companies use a structure within a structure to run their business – this was of no consequence to me as relevant documentation was provided."

and at paragraph 13 he stated that:

> "The invoice from Quadrant detailing a separate company did not cause concern as the VAT number matched the company name. I understood that Quadrant were the parent company in respect of UX-Ray and Decent Solutions."

44. On being asked about these two companies, he told the Tribunal that:

> "I thought the companies used were under the control of Mead" and "I was unperturbed as they were under Mead's control"

and later when the apparent contradiction was put to him:

> "All I knew was Mead was part of Quadrant. I was not sure about the company structure. I am not sure why I said the companies were under the control of Mead".

At best, this does not sit well with his assertion that he had done a lot of due diligence.

45. Mr Sheffield confirmed that he had been aware of the existence of UX-Ray LIMITED and that he had asked Mr Jones about it and had been told that it was one of the group of companies in the Quadrant Group. He could not recall when he had asked but he assumed that it had been before the First Agreement was signed on 1 October 2013 as he was "fairly certain" that Mr Jones had supplied the copy VAT registration certificate dated 24 July 2013.

46. Mr Sheffield was unable to explain why he thought that that company would be providing payroll services, including the provision of labour, when the business activity description on the VAT certificate was "Management consultancy activities other than financial management".

47. He was equally unable to explain why he had entered into contracts with Mead if he knew he was dealing with UX-Ray LIMITED.

48. His only explanation was that he had no reason to care which company provided the labour force or payroll because he had done a lot of due diligence. He certainly does not appear to have paid any attention to which company was involved at any stage and nor does it seem that he has done even minimal due diligence to the standard that would be expected of a prudent trader.

49. He was also vague as far as Decent Solutions Limited was concerned. He said that he could not recall when the change occurred to Decent Solutions Limited but since there was an invoice in the bundle dated 27 April 2015, it was at least by that date and Mead Outsourcing was still the payee. He could not explain when or why that had changed.

50. Effectively the only explanation he could offer was that Mr Jones had told him that Decent Solutions Limited was one of the group companies and was a valid trading company.

51. He could not explain why there was no written assignation in terms of Clause 19.2 of the First Agreement (see paragraph 13 above).

52. There were other areas where there was a startling lack of clarity. Mr Sheffield was wholly unable to explain why, when his own staff had told HMRC on 28 August 2014 that HMRC had told them that Red Management Catering Limited had ceased to exist in 2011, he had told HMRC on 23 February 2016 that the payroll service was provided by Red Management Catering. (He certainly could not reconcile that with his comments on the other companies.)

53. Paragraph 11 of the appellant's Skeleton Argument argued that the Quadrant Group was involved in human resources issues and as an example Mr Jones had acted as the appeal officer for a grievance hearing. Mr Sheffield could not explain why Mr Jones was described in the Minutes as being present for "Red Management".

54. He could not explain why, in that capacity, Mr Jones had told the employee that the primary thing that had legally changed was "the PAYE reference" and that the reason that the outsourcing had been done was for "… financial restructuring for the business … if in the event of any disputes etc the staff would simply be TUPE'd back into Symphony Hotel."

55. Ultimately, Mr Sheffield's default position was that he had relied heavily on Mr Jones. If Mr Sheffield is to be believed he relied entirely on Mr Jones and even in the face of the warning letter from HMRC about UX-Ray LIMITED he continued to pay invoices and reclaim the VAT in the knowledge that that was wrong. Quite why he apparently believed Mr Jones' alleged reassurance about UX-Ray LIMITED is a mystery.

56. Although he knew about the deregistration of UX-Ray LIMITED, when he received the warning about the tax loss in the supply chain for Decent Solutions Limited he had done none of the due diligence suggested in the accompanying leaflet because Mr Jones had apparently reassured him that everything was in order.

57. He eventually conceded that he had never asked Mr Jones about the group structure and argued that he had built up a relationship with him when asking for HR advice, such as in the appeal hearing, and he had not wanted to "interrogate" him. In itself, that argument did not sit well with paragraph 2 of his own witness statement which said that he had "… vast experience" in handling potential HR issues.

58. Mr Jones had allegedly told him that he did not need to change the contracts of employment for the staff. There was no evidence that anyone recruited after 1 October 2013 had their contract of employment assigned although possibly it was a matter of verbal agreement with Mr Jones. On the balance of probability I find that they were simply added to the payroll.

59. At all times, the employees were recruited, managed and dismissed by the appellant.

60. On the balance of probability, Mr Jones was correct in stating that the reality was that all that changed after 1 October 2013 was the PAYE reference. If the third agreement had been implemented then that is literally all that would have changed. I understand why

HMRC argue in their Skeleton Argument that "… the staff are employed by the appellant". The staff certainly believed that to be the case.

61. Since the third agreement was not implemented the only other change was that instead of operating the payroll, the appellant sent Quadrant Services (UK) details of the salaries and hours worked before the due date for payment, the appellant paid Quadrant the net wages and a company, presumably in the Quadrant group, then paid the employees and at the end of the period Quadrant reconciled the PAYE and NIC, added a service charge and invoiced the appellant for the balance due.

62. The supply of staff is a taxable supply of services to which the standard rate of VAT applies.

63. Section 4(1) VAT Act 1994 states:-

> "VAT should be charged on any supply of goods or services made in the UK, where it is a taxable supply made by a taxable person in the course or furtherance of any business carried on by him."

64. I simply do not accept the argument that Mead novated the contract to UX-Ray Limited and then to Decent Solutions Limited. To the limited extent that Mr Sheffield is credible, it seems likely that he was aware of the existence of UX-Ray LIMITED prior to signing the First Agreement (see paragraph 45 above) but he chose to contract with Mead.

65. I accept Officer Drummond's commendably clear and straightforward explanation that her concern was whether or not either UX-Ray LIMITED or Decent Solutions Limited had made any supplies of labour to the appellant. I find that there is no credible evidence of any such supply.

66. In summary, at best, the appellant outsourced its staff to Mead, with effect from 1 October 2013, although no member of staff was aware of that and new members of staff had every reason to believe that their employer was the appellant. The only party who could have issued valid VAT invoices would have been Mead.

67. I have no hesitation in finding that there were no valid VAT invoices for the supply of labour in the periods in question.

68. The remaining issue is whether or not there is sufficient evidence to prove that the substantive requirements for obtaining a deduction are met in the absence of valid VAT invoices.

69. I am bound by, and indeed agree with, the decision of the Upper Tribunal in *Scandico Limited v HMRC*[1] where at paragraph 43 the Tribunal stated:

> "In appeals of this kind, the First-tier tribunal should address only the decision which is before it, namely HMRC's decision that, in the absence of the VAT receipts, they were not prepared to exercise their discretion to accept the alternative evidence provided by the taxpayer as to whether there had been a taxable supply. The test that the First-tier tribunal applies in reviewing that decision is the test set out in *Kohanzad*[2]."

70. That test is narrated in *Scandico* at paragraph 19 which reads:

> "19. Schiemann J went on to say:-
>
> 'It is established that the Tribunal, when it is considering a case where the commissioners have a discretion, exercises a supervisory jurisdiction over the exercise by the commissioners of that discretion. It is not an original discretion of the tribunal, it is one where it sees whether the commissioners have exercised their discretion in a defensible manner. That is the accepted law in this branch of the court's

[1] [2017] UKUT 467 (TCC)
[2] *v Customs and Excise Commissioners* [1994] STC 967

> jurisdiction and it is recently been decided that the supervisory jurisdiction is to be exercised in relation to materials which were before the commissioners, rather than in relation to later material.'"

71. I find that, in the circumstances narrated above, Officer Drummond very reasonably found that she had no evidence that either UX-Ray LIMITED or Decent Solutions Limited had made any supply of labour to the appellant.

72. That being the case, although undoubtedly the staff worked for the appellant, I do not accept that that in itself demonstrates that they were provided by either of those companies.

73. Accordingly the appellant is not entitled to deduct the input VAT that it has been charged and has paid in relation to the purported supplies of staff. The acknowledged inadequacies in the documentary evidence are certainly not compensated for by other evidence of the facts. Indeed the facts of the matter are decidedly opaque.

Decision

74. I therefore uphold HMRC's decision to issue assessments and amend the amounts shown on the 01/15 return and I dismiss the appeal.

Right to apply for permission to appeal

75. This document contains full findings of fact and reasons for the decision. Any party dissatisfied with this decision has a right to apply for permission to appeal against it pursuant to Rule 39 of the Tribunal Procedure (First-tier Tribunal) (Tax Chamber) Rules 2009. The application must be received by this Tribunal not later than 56 days after this decision is sent to that party. The parties are referred to "Guidance to accompany a Decision from the First-tier Tribunal (Tax Chamber)" which accompanies and forms part of this decision notice.

ANNE SCOTT
TRIBUNAL JUDGE

RELEASE DATE: 24 MAY 2019